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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

JUN 27 1994

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of

Implementation of Sections of
the Cable Television Consumer
Protection and Competition Act
of 1992

Rate Regulation

and

Adoption of a Uniform Accounting
System for Provision of Regulated
Cable Service

MM Docket No. 93-215 ✓

CS Docket No. 94-28

REPLY OF COMCAST CABLE COMMUNICATIONS, INC.

Comcast Cable Communications, Inc. ("Comcast"), by its attorneys, hereby responds to certain oppositions to its petition for reconsideration filed in the above-referenced matter. Comcast believes the public interest is not served by rules that retroactively penalize cable operators for investments that occurred prior to regulation and fail to account for the financial realities operators face today. The Commission must reject those oppositions that seek to impose unjustified regulatory burdens on cable operators. Rather, the Commission should adopt rules that reflect the fundamentals of the cable industry and provide cable operators with the opportunity to recover and earn a fair return on their pre-regulation investments. Although the solutions proposed by Continental Cablevision, et al. ("Continental") and the United States Telephone Association ("USTA") are helpful and superior to the rules adopted by the Commission,

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List A B C D E

Comcast believes that only full recovery of and return on pre-regulation investment in tangible and intangible assets completely satisfies constitutional standards.

I. THE COMMISSION MUST PERMIT OPERATORS TO RECOVER AND EARN A RETURN ON THEIR NET INVESTMENT IN TANGIBLE AND INTANGIBLE ASSETS

There is almost universal agreement that the Commission's treatment of intangible assets acquired by a cable operator is administratively burdensome and may produce results that are confiscatory.^{1/} As stated by USTA, "this set of presumptions is ambiguous, complex and probably unworkable in local rate setting proceedings." Response of USTA at 10. In order to satisfy constitutional standards the Commission must amend its rules to include a transition mechanism that permits operators to recover and earn a fair return on

^{1/} NATOA argues that there is "no reason whatsoever" for including intangible assets in the ratebase. As discussed below, if the local authorities represented by NATOA were to adopt this unyielding interpretation of the Commission's presumptions, a blanket stay on all local cost of service decisions would be necessary to avoid rates so low that operators would be unable to repay the debt for their systems. Bell Atlantic opposes inclusion of "excess acquisition costs" and states that this investment should be recovered from unregulated services. It is ironic that Bell Atlantic and other LECs continually argue that they are unfairly required to subsidize residential service with revenues from other services even as they advocate that regulated cable service should be subsidized by unregulated services.

their pre-regulation investments in tangible (including the stepped-up basis) and intangible assets.^{2/}

Continental proposes that operators be permitted to include 66 percent of the gross purchase price of an acquired system in the ratebase.

Response of Continental at 6. Continental also proposes that accumulated losses from early years of operation should be treated as additional investment in the system and added to the ratebase. *Id.* at 8. USTA suggests that operators be permitted to amortize, but not earn a return on, their pre-regulation investment in acquired intangible assets.^{3/}

While the proposals advanced by Continental and USTA are superior to the current rules, both proposals understate the return that operators

^{2/} Bell Atlantic's statement that exclusion of pre-regulation investments is "standard regulatory practice" is grossly misleading. Bell Atlantic cites its Joint Reply Comments "and cases cited therein" to support this proposition. However, the only case cited in the Joint Reply Comments is an FCC decision regarding the ratebase of dominant telephone companies and the potential for abuse presented by the "acquisition by one utility of the property of another utility." Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, 3 FCC Rcd 269, 273 (1987) (emphasis added). At no point in this proceeding has Bell Atlantic cited any precedent from any regulated field that supports the notion that it is "standard practice" to deny retroactively recovery of and a return on investments made before a company becomes regulated as a utility.

^{3/} Response of USTA at 10-12. As discussed below, the Commission must reject the notion that a transition mechanism (or any other component of the cost of service rules) should be structured to achieve regulatory parity between cable operators and LECs. Moreover, to the extent USTA seeks to deny recovery of "excess acquisition premiums", the Commission should impose the burden of proving such premiums on the regulatory body that reviews a cost of service showing.

should be allowed to earn. The USTA proposal, for example, is the equivalent of allowing cable operators to get repaid only for the principal on their debt with no provision for interest. This approach would leave little or no room for any return on equity and, in many cases, will be insufficient to satisfy constitutional standards. Similarly, the Continental approach may be unsatisfactory when a 66 percent return on the gross purchase price is insufficient to cover the debt associated with the acquisition.

The Commission must respect the financing arrangements upon which the growth of the cable industry has been based. Prior to regulation lenders relied on the value of all the assets of an acquired system and they demand a return on their entire investment, notwithstanding the regulatory regime imposed by the Commission. Accordingly, operators must be permitted to recover their investment in and earn a return on the stepped-up basis of acquired tangible and intangible assets, as well as accumulated losses.^{4/}

Comcast submits that the approach proposed in its Petition is superior to the proposals advanced by USTA and Continental. The Comcast approach recognizes the importance of intangible assets to all businesses and ensures that operators will earn revenue sufficient to make debt payments that were lawfully incurred prior to regulation. Moreover, by phasing in rate

^{4/} Petition of Comcast at 17. As discussed below, Comcast stands by its conclusion that adoption of the same rate of return for two entirely distinct industries, one of which has the risk associated with high debt ratios, is unjustified.

adjustments over time, the Comcast approach has the benefit of protecting consumers from paying unreasonable rates. The transition mechanism proposed by Comcast in its Petition strikes the proper balance between the interests of consumers and operators and should be adopted by the Commission.

II. THE COMMISSION SHOULD STAY ENFORCEMENT OF ALL LOCAL COST OF SERVICE DECISIONS PENDING RECONSIDERATION

It is common regulatory practice to permit rate increases to go into effect (subject to an accounting order) while the resolution of a rate case is pending. This allows service providers to charge compensatory rates while protecting subscribers if those rates are ultimately held to be unreasonable.^{5/} For the same reason, Comcast believes that orders of local franchising authorities prescribing rate reductions should be stayed pending appeal.

As discussed above, the Commission's presumptions regarding intangible assets make it likely that operators will be ordered to take significant rate reductions. Moreover, NATOA and its members apparently have no inclination to permit a return on or recovery of intangible assets regardless of the results such a policy would produce.^{6/} Because of the harsh results the cost of

^{5/} See, e.g., Transcontinental Gas Pipe Line Corp. v. F.E.R.C., 866 F.2d 477, 481 (D.C. Cir. 1988); Papago Tribal Utility Authority v. F.E.R.C., 628 F.2d 235 (D.C. Cir. 1980), cert. denied, 449 U.S. 1061 (1980).

^{6/} NATOA's position leaves no room to overturn the Commission's presumptions: "[T]here is no reason whatsoever for cable subscribers to pay
(continued...)

service rules will produce, most operators can be expected to appeal local cost of service decisions.

Under the cost of service rules, local authorities have no obligation to stay rate reductions while an appeal of a local rate decision is pending. Consequently, in order to avoid irreparable injury, an operator that appeals a local decision also must petition the Commission for a stay of that decision pending review by the Commission. Because of the time required for an appeal (the Commission has not yet decided a single cable programming complaint or appeal of a local rate case) and the magnitude of potential rate reductions, failure to obtain a stay could seriously threaten the viability of a system.

The process of requesting a stay for all local cost of service decisions is administratively burdensome and expensive for operators, regulators and consumers. Furthermore, operators challenging local cost of service decisions will almost always be able to satisfy the traditional requirements for a stay.^{7/} In order to spare all parties the expense of litigating the inevitable stay requests that

6/ (...continued)

higher rates to allow an operator to recover such intangible costs." Opposition of NATOA at 7.

7/ See Virginia Petroleum Jobbers Assoc. v. F.P.C., 259 F.2d 921 (D.C. Cir. 1958). The Commission must consider the following four factors in a stay request: (1) the likelihood of success on the merits; (2) whether there will be irreparable injury absent a stay; (3) whether a stay will harm other parties; and (4) whether it is in the public interest. The breadth of support for changes to the cost of service rules demonstrates that an operator challenging the rules is likely to prevail on the merits. Combined with the fact that the injury caused by a rate reduction will always be irreparable, a stay should be granted in almost all cases.

will arise under the cost of service rules, the Commission should immediately impose a blanket stay, and corresponding accounting order, on all local enforcement decisions based on the exclusion from the ratebase of acquired tangible and intangible assets. The stay and accounting order should remain in effect until the Commission adopts a transition mechanism that permits recovery of and return on pre-regulation investments.

III. REGULATORY PARITY IS NOT AN APPROPRIATE GOAL FOR CABLE COST OF SERVICE RULES

In its Petition, Comcast requested that the Commission reconsider its decision to adopt a rate of return for cable operators equal to the rate used for telephone companies. Petition of Comcast at 18. Comcast showed that the Commission did not adequately consider the business risks faced by cable operators (including the risks created by the Commission's implementation of the 1992 Cable Act) and that imposing the rate of return established for telephone companies is arbitrary and capricious.^{8/}

^{8/} The charge that LECs are subject to greater risk from competition than cable operators is ludicrous. USTA's statement that "neither technical nor regulatory barriers stand in the way of cable companies competing with local exchange carriers" is so far off base that it barely merits a response. Facilities-based telecommunications competition is likely to develop more slowly now that federal interconnection rules have been struck down. Moreover, formidable technical and legal barriers to entry still prohibit local exchange competition. Bell Atlantic, on the other hand, has applications pending to provide video dialtone service to over 3 million subscribers throughout its service area and it is not presently constrained by the telco/cable cross-ownership prohibition.

In response, Bell Atlantic, GTE and USTA argue that telephone companies and cable companies must be subject to symmetrical regulatory regimes, including similar rates of return. Response of USTA at 13; Opposition of Bell Atlantic at 3-4; Comments of GTE at 9. The telephone companies have raised this argument repeatedly over the last two years and repeatedly it has been rejected.^{9/} The telephone companies once again are attempting to transform a proceeding on cable issues into a forum for their incessant complaints about the price cap rules for local exchange carriers. To the extent new issues are raised by the telephone companies, these issues should be addressed in the LEC Price Cap Review^{10/} and have no place in this proceeding.^{11/}

Not only is the regulatory parity argument advanced by the telephone companies out of place in this proceeding, it is bad public policy. Regulation of a particular market must be based on the presence of market power

9/ "Telephone companies have failed to advance a sufficient reason why we should adopt as an overriding policy goal achieving regulatory parity." First Order on Reconsideration, MM Docket No. 92-266, FCC 93-428 at ¶ 90 (rel. Aug. 27, 1993); see also Opposition of the National Cable Television Association at 5 n.5 (listing seven pleadings in which Bell Atlantic has requested regulatory parity since January 1993).

10/ Price Cap Performance Review for Local Exchange Carriers, Notice of Proposed Rulemaking, 9 FCC Rcd ____ (1994).

11/ As demonstrated by Continental, the telephone companies only want "parity" for regulations they perceive to place a greater burden on LECs than on cable operators. They are conspicuously silent with regard to burdens placed on cable operators but not on LECs. Response of Continental at 15 n.31. Bell Atlantic, in fact, has vigorously opposed imposition of any cable obligations, including franchising, on its video programming operations. See Opposition of Chesapeake and Potomac Telephone Co. of Virginia, W-P-C 6834, filed Jan. 10, 1994 at 11-14.

and the legal, technical and economic barriers to entry that perpetuate that market power. The Commission has correctly recognized that it only should pursue the goal of parity for similarly situated companies in the same market. Thus, equal treatment of CMRS providers or nondominant carriers is appropriate based on the Commission's analysis of those particular markets. Conversely, to suggest that companies in different markets should be subject to regulatory parity because those markets may converge in the future is absurd, particularly given the enormous differences between the statutory regimes that apply to cable and telephony.^{12/}

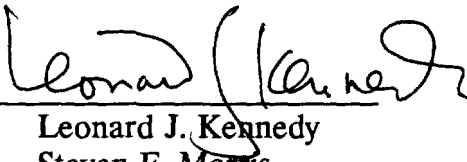
^{12/} Moreover, as demonstrated by Discovery Communications, complete regulatory parity would undermine the Commission's goal of fostering quality programming at reasonable rates. Opposition of Discovery Communications at 3.

IV. CONCLUSION

The Commission should adopt the transition mechanism proposed by Comcast to permit operators to recover and earn a return on their investment in tangible and intangible assets acquired prior to regulation. The rate of return on these investments should be based on the realities of the cable industry, not on baseless requests for regulatory parity. Until the Commission adopts these changes, it should impose a blanket stay on all local cost of service decisions that are based on the exclusion from the ratebase of any pre-regulation investment.

Respectfully submitted,

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June 27, 1994

CERTIFICATE OF SERVICE

I Roberta L. Fidele hereby certify that on 27th day of June, 1994 that a copy of the foregoing **REPLY OF COMCAST CABLE COMMUNICATIONS, INC.** was served upon the following via first class mail, postage prepaid to the following:

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